

Libey Economic Outlook

September 2007

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Published Exclusively For Clients Of

Libey Incorporated

Advisors & Recruiters to Multichannel Direct Marketing

Cherry Hill, New Jersey

www.libey.com

Pricing

Don Libey

I believe pricing is going to be a significant factor in 2008. Prices must increase because everything else is poised to increase. This time, however, it may require a different approach to increasing prices.

I don't know of anyone today who is a Master Pricer. Most of us in multichannel marketing consider pricing to be the domain of the merchandisers; it is a function of sourcing, margin, competition, etc. We tend to view it as a linear process. If a product costs x and competitively sells for y , then we price it at z . Our price strategy is to be one of three places: the top, the middle or the bottom. Linear. Cut and dry. But, it is much more complex than today's simplistic approach.

Once, I worked for a Master Pricer. He was the CEO of a three-quarters of a billion dollar company that (back in the 70s) sold via a field sales force, inside telemarketing or 'inside sales' as it was called, a series of nine different catalogs and other direct mail, and three separate dealer organizations. My job was running the direct marketing and dealer organizations. The company manufactured all of its products (business forms) and it had six plants in four states and two countries. There were about 2,000 employees.

At that scale, you would imagine the CEO was occupied at all levels and spent his time meeting with senior executives and plant managers. Not really. What he did—and very successfully—was to delegate all of the operations of the business to talented managers. He sat in his office all day, every day with a completely clear desk and reviewed and priced *every* order.

Now, this was a company with almost 600 sales people on the street. Every one of them sent their orders to the CEO for pricing and he talked over every order with each sales person. By the time a price was determined (and it was fast), the CEO and the sales person had reviewed competitive prices from other manufacturers, account history, past pricing, usage rates, annual sales volume, re-order rates, margins, sales commissions, and every other detail that could or would influence the pricing decision.

Every price was custom; every price was maximized for margin, competitive position and maintaining the customer. I was the lucky one at that company. Since my overall sales from catalogs and dealers were under \$80 million, I was allowed to do my own pricing and run my own show. However, my \$80 million in sales produced a contribution to overhead that was double the percentage rate of the CEO. He liked that and left me alone. I was the guaranteed \$10 million of earnings he had in the bag every year to make the overall business look good. My little catalog and dealer business was, essentially, a slush-fund.

I tried to learn how he priced product. There were no tables or price lists, no discounted columns, no 'right column' prices, no competitive comparison lists. Each transaction consisted of a customer, a product, a quantity, a cost, a sales commission, and the next order. Six elements. His thinking seemed to go through a pattern as follows:

1. What do I need to make an acceptable margin given my costs?
2. How does this product influence my margin; can I get more or less profit?
3. What is the cost of commission and is that fair to the company, the customer and the salesperson?
4. What if the quantity was smaller or greater, either now or on future orders?
5. What is the likely competitive price?
6. What does it take to retain the customer and grow the volume?

These six 'analytics' produced a conclusion. Remember, the CEO had six plants to keep running. Business forms production at that scale is calculated in tonnage. Huge presses are kept running around the clock. And they have to produce a margin. His conclusions consistently produced some of the highest earnings in the business forms industry. He was a Master Pricer and that was his great strength. He controlled—absolutely—the margins and the earnings through individualized pricing on every order.

Now, reflect on how he had established various strategic components of the overall business. He had 600 sales people driving solid margin, high volume business. He paid four or five of those sales people more money in commissions than he earned as CEO, and he was happy to do it. But, when a customer's volume dropped and the threshold margin no longer could support outside sales, he moved that customer to inside sales and a telephone account representative at a different but acceptable margin for inside sales. That forced the outside sales person to beat the street and find a replacement for the lost customer and commissions. The company won. The company always won.

Whenever a customer's inside sales volume dropped, that customer was moved to the dealer division or the catalog division. Again, acceptable margins on lower volume,

and the forcing of other customers into inside sales and the need to recruit new customers on the street. This was a beautiful, closed system that kept pressure on the sales force to constantly find newer and bigger customers. And it worked like a fine watch.

One can say this company was manufacturing driven, or sales driven, or marketing driven, or perhaps (for the 1970s) even multichannel driven. I believe it was truly price driven. The CEO's abilities as a Master Pricer was what kept the process bubbling. He was like a starter yeast for good bread. Once he priced a product, it was either for the company's profitability or for the re-positioning of the customer and the maximization of selling time and energy in recruiting new and bigger customers. Of course, there was a drawback: he was the only one who understood the process. But, his objective became clear one day. When it was time to retire, he had built a \$750 million public company and it was sold to its primary competitor at a huge multiple of substantial earnings and everyone went home wealthy.

What he knew about every price was the customer, the volume, the sales person's abilities, and where the customer was best retained. And, he knew his costs . . . cold. He was a Master. Perhaps some of that mastery can and should be applied to our multichannel experience of 2008. I am convinced that pricing in the near-term is going to become exceptionally important and that linear models are not going to work. Maybe what my old CEO has left as a valued legacy is the opportunity to *think* about pricing in a different way and in a different context than we have for the last ten years or so.

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New Books

MeritDirect Press is publishing a second, revised addition of *Libey and Pickering on RFM and Beyond*. This new addition will feature new chapters extending Christopher Pickering's work in multichannel understanding and incorporating new, up-to-the-minute thinking about the analytics of advanced direct marketing. As a co-author, I will add new thoughts on the foundation elements necessary for success in the increasingly difficult economic environment of the coming years. The new edition is scheduled for release in mid-December of this year.

Direct Academy is publishing Kevin Hillstrom's second book, *Hillstrom's Multichannel Forensics* this month. This is the long-awaited companion to Kevin's first book, *Hillstrom's Database Marketing* and looks at the migration of customers in, around and between channels. As the publisher, I can only promise you one of the most fascinating books on customer behavior and analytics I have ever read.

Direct Academy has also reprinted Kevin's first book, a most welcome event because, thankfully, the first printing of the book has sold out. All three books will be available at the publisher's site, www.forbetterbooks.com, on Kevin Hillstrom's website www.minethatdata.blogspot.com, or on the MeritDirect website www.meritdirect.com. Books are also available through Amazon, Barnes & Noble, or your favorite bookshop (we would prefer that you purchase from us directly, however).

Comptroller of the United States, David M. Walker: View of the U.S. Economic Future

The following article was only given visibility in Europe. David M. Walker is a highly credible individual with impeccable credentials. He is the Comptroller General of the United States, a non-partisan position charged with providing Congress with the truth. It makes for rather sobering reading as we ponder the future leadership of the nation and our economic destiny.

Comptroller General Compares US to Roman Empire

by Financial Times repost

Tuesday Aug 14th, 2007 7:53 AM

The US government is on a ‘burning platform’ of unsustainable policies and practices with fiscal deficits, chronic healthcare under funding, immigration and overseas military commitments threatening a crisis if action is not taken soon, the country’s top government inspector has warned. David Walker, Comptroller General of the US, issued the unusually downbeat assessment of his country’s future in a report that lays out what he called “chilling long-term simulations”. These include “dramatic” tax increases, slashed government services and the large-scale dumping by foreign governments of holdings of US debt.

Drawing parallels with the end of the Roman Empire, Mr. Walker warned there were “striking similarities” between America’s current situation and the factors that brought down Rome, including “declining moral values and political civility at home, an over-confident and over-extended military in foreign lands and fiscal irresponsibility by the central government.”

“Sound familiar?” Mr. Walker said. “In my view, it’s time to learn from history and take steps to ensure the American Republic is the first to stand the test of time.”

Mr. Walker’s views carry weight because he is a non-partisan figure in charge of the Government Accountability Office, the investigative arm of the US Congress.

While most of its studies are commissioned by legislators, about 10 per cent – such as the one containing his latest warnings – are initiated by the Comptroller General himself.

In an interview with the Financial Times, Mr. Walker said he had mentioned some of the issues before but now wanted to “turn up the volume.” Some of them were too sensitive for others in government to “have their name associated with.”

“I’m trying to sound an alarm and issue a wake-up call,” he said. “As Comptroller General I’ve got an ability to look longer-range and take on issues that others may be hesitant, and in many cases may not be in a position, to take on.”

“One of the concerns is obviously we are a great country but we face major sustainability challenges that we are not taking seriously enough,” said Mr. Walker, who was appointed

during the Clinton administration to the post, which carries a 15-year term.

The fiscal imbalance meant the US was “on a path toward an explosion of debt.”

“With the looming retirement of baby boomers, spiraling healthcare costs, plummeting savings rates and increasing reliance on foreign lenders, we face unprecedented fiscal risks,” said Mr. Walker.

Current US policy on education, energy, the environment, immigration and Iraq also was on an “unsustainable path.”

“Our very prosperity is placing greater demands on our physical infrastructure. Billions of dollars will be needed to modernize everything from highways and airports to water and sewage systems. The recent bridge collapse in Minneapolis was a sobering wake-up call.”

Mr. Walker said he would offer to brief the would-be presidential candidates next spring.

“They need to make fiscal responsibility and inter-generational equity one of their top priorities. If they do, I think we have a chance to turn this around but if they don’t, I think the risk of a serious crisis rises considerably”.

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Is this an alarmist’s view? I doubt it, as Mr. Walker is well-respected by economists, bankers, government officials, world leaders, even members of Congress. He has no history of “Chicken Little-ism.” His writings throughout his long and distinguished career are sound, accurate and uncompromising. He is an individual of great integrity and intelligence. He is probably the best governmental appointment Bill Clinton ever made. And, he is an accountant.

Most of us, in those quiet moments of rational reflection, would question the direction and priorities of the American economic strategy. We would question them rightfully because, if we applied identical strategies to our business economics, we would doubtless be shortly bankrupt.

At stake here is the supremacy of the global currency. We are engaged in a battle between the Euro, the Dollar and the Yuan. The financial center of the world is shifting from New York to London. The great bourses are joining into a collective, digital global market. The economic growth of nations has dramatically reversed in just the past decade. These future economic outcomes will play out in the next twenty years, perhaps sooner. And, like or not, care to talk about it or not, but the truth has been stated by Mr. Walker.

We may well be coming to a time—as we did in the 1940s—when the American spirit will be called upon and tested. If it is to be so, then our greatest strength will lie in the preparation of our business foundations, in the strength of our individual company’s economic engine, in the solidity of our competitive positions in the markets.

There will likely be a new economic skeleton for U.S. commerce. My view is that it will be beneficial and rejuvenating. As we engage on the very real problems outlined by Mr. Walker, we will, by necessity, find new business and civic models that will redistribute economic resources in a sustaining manner. When we emerge from the years of U.S. re-engineering, I believe we will have in place the elements needed for the next 100 years. Part of those elements will be a redefined government, part a redefined system of taxation, part a redefined social entitlement structure, part a redefined health delivery system, part a redefined educational system, and—a big part—a redefined U.S. global role. From that lengthy period of massive redefinition will emerge a stronger, self-sustaining America.

I see the coming period of redefinition not as a dire crisis, but rather a normal evolution of our society. It is change. I also see the necessity for strengthening our businesses to withstand the effects of change. That is why my keynote at the MeritDirect Co-Op, *The Twenty Pillars for Performance and Profitability* seemed to strike a chord for many (at least based on the emails I have received in the last 30 days). We are entering a period of strengthening, of redesigning, of streamlining, of building new foundations for an even larger future on a global basis. These are—truly—the worst of times and the best of times.



The Fourth Quarter 2007 Economic Outlook

As of late August, increased caution continues to be called for due to the emerging economic performance indicators. The subprime mortgage difficulties are probably deeper than first thought and the effects on the international credit markets have been surprising. The very real potential of a burst in the private equity bubble that we mentioned last issue seems to be materializing as numerous deals are being refinanced, postponed or abandoned due to the higher cost of money and a lower tolerance for risk. In the end, it is always all about banks; now, it is banks on a global scale.

The political struggles of the deathless campaigns are, in my estimation, causing the Congress and the administration to ‘spin control’ the economic outlook so we get through the election before the unpleasant reality is released on the unwitting public. The problem is that this is fourteen months away, an economic lifetime. Denial is dangerous.

The energy, war, deficit spending, trade deficit, immigration, aging, health care, crumbling infrastructure, climate change and other purely domestic issues are exerting huge pressures on the American economy and *nobody is dealing with the problems*. They are not going to go away. The only potential answer is increased and ever-increasing taxes, no matter what the politicians say. The alternative is truly scary.

My view, going soon into the fourth quarter, is that the holiday season will be constrained for consumers. Less money will be spent this year as the “petroleum season” heats up and money is spent on more costly necessities. The housing market is not recovering and debt has, for the first time, moved the nation into a negative savings rate. Simply put, there is less money to be spent.

Businesses are beginning to move to a more cautious outlook, as well. At some point, we all must recognize that the engine of the American economy is consumer spending in all its myriad forms. When that spending slows, the business economy slows as a result. My estimate is that many business-to-business direct companies will see less than 6 percent growth by year end. Actually, 6 percent would be acceptable in the face of an overall economy that may not top 2 percent growth for 2007.

We are also beginning to understand the effect of the 2007 postage increase and the shift in advertising allocation that is underway. I would also suggest that the USPS will seek another rate increase perhaps of the same size as the 2007 sledge hammer. Even with the recent increase, the USPS posted a nearly half-billion dollar loss. It’s a fairly simple formula: either Congress or you will pay for that. Congress won’t raise taxes in an election cycle, so that leaves you. Again, you have to take an active stand and fight for your welfare.

Signs of Regional Stability or Status Quo

Region One (CT, ME, MA, NH, RI, VT)
Region Two (NY, NJ, CT, PR, VI)
Region Four (OH, KY, PA, WV)
Region Six (GA, AL, FL, LA, MS, TN)
Region Seven (IL, IN, MI, WI, IA)
Region Nine (MN, WI, ND, SD, MT, MI)
Region Ten (KS, CO, MO, NE, NM, OK, WY)
Region Twelve (CA, UT, AZ, NM, OR, WA)

Slower

Region Three (PA, NJ, DE)
Region Five (KY, MD, TN, VA, NC, SC)
Region Eight (MO, IL, IN, KY, TN, LA, AR)
Region Eleven (TX, LA, NM)

Evaluate individually

**Louisiana
Mississippi**

The Fourth Quarter 2007

Circulation and Prospecting Outlook and Recommendations

Synopsis

The short-term economic outlook for the catalog industry remains positive. The intermediate-term outlook remains positive for the fourth quarter of 2007 and the long-term outlook into 2008 remains positive. While positive, the outlook is also for slower growth.

Prospect as an Investment

For the fourth quarter 2007, even with the signs of slowdown in the economy and in overall business, we recommend maintaining normal strategies for circulation and investment prospecting plans, but likely not more than 10 to 15 percent increases. The economy is going to slow further in the fourth quarter, but there are still no indications or good reasons for reductions in either prospecting or customer circulation, or both, in the last quarter of the year or the early part of 2008. We would remain comfortable with modest increases in prospecting levels, particularly where small pockets of concentrated niche-related prospects can be found.

Nation at a Glance

We will stick to our mailing recommendations for fourth quarter planning in 2007 and first quarter planning for 2008. We caution against decreasing prospecting or customer mailings except for normal hygiene and mailing frequency improvements. Do not fall into the trap of reducing mailings; the end result is always diminished customer acquisition performance. Changes are in **bold**.

State	Mailings		
		Indiana—South	Normal
		Iowa	Increase
		Kansas	Normal
Alabama	Normal	Kentucky—East	Normal
Alaska	Normal	Kentucky—West	Normal
Arizona	Normal	Louisiana—North	Evaluate locally
Arkansas	Normal	Louisiana—South	Evaluate locally
California	Increase	Maine	Normal
Colorado	Increase	Maryland	Increase
Connecticut	Increase	Massachusetts	Increase
Connecticut-Fairfield	Increase	Michigan	Normal
Delaware	Normal	Michigan—Up. Pen.	Normal
District of Columbia	Normal	Minnesota	Increase
Florida	Normal	Mississippi—North	Evaluate locally
Georgia	Normal	Mississippi—South	Evaluate locally
Hawaii	Normal	Missouri—North	Normal
Idaho	Normal	Missouri—South	Normal
Illinois—North	Normal	Montana	Normal
Illinois—South	Normal	Nebraska	Normal
Indiana—North	Normal		

Nevada	Increase	South Carolina	Normal
New Hampshire	Normal	South Dakota	Normal
New Jersey—North	Increase	Tennessee—East	Normal
New Jersey—South	Increase	Tennessee—West	Normal
New Mexico—East	Normal	Texas	Normal
New Mexico—West	Normal	Utah	Normal
New York	Normal	Vermont	Normal
North Carolina	Increase	Virgin Islands	Normal
North Dakota	Normal	Virginia	Normal
Ohio	Normal	Washington	Increase
Oklahoma	Normal	West Virginia—East	Normal
Oregon	Increase	West Virginia—West	Normal
Pennsylvania—East	Normal	Wisconsin—North	Increase
Pennsylvania—West	Normal	Wisconsin—South	Increase
Puerto Rico	Normal	Wyoming	Normal
Rhode Island	Normal		

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